

GAO

United States General Accounting Office
Report to Congressional Requesters

June 1996

**TAX
ADMINISTRATION**

**IRS' Interpretative
Guidance
Implementing the Tax
Reform Act**





United States
General Accounting Office
Washington, D.C. 20548

General Government Division

B-137762

June 19, 1989

The Honorable Dan Rostenkowski
Chairman, Joint Committee on
Taxation

The Honorable Lloyd Bentsen
Vice Chairman, Joint Committee
on Taxation
Congress of the United States

The Honorable J. J. Pickle
Chairman, Subcommittee on Oversight
Committee on Ways and Means
House of Representatives

This report responds to your requests for information on interpretative guidance the Internal Revenue Service (IRS) and Department of the Treasury provided to taxpayers in implementing the Tax Reform Act of 1986 (Public Law 99-514). Such guidance includes published regulations (proposed, temporary, or final), revenue rulings, revenue procedures, notices, and announcements describing IRS interpretations of Internal Revenue Code provisions.

You specifically asked that we report on (1) IRS' priorities for providing the interpretative guidance, (2) the status of IRS' publication of the guidance, (3) any problems encountered in providing the guidance in time for the 1988 filing season (before January 1988), and (4) any guidance that was unavailable for the filing season. You also asked how IRS had applied the lessons it learned from issuing a revised Form W-4 (Employee's Withholding Allowance Certificate) without obtaining comments from the general public.

Background

IRS primarily relies on regulations, revenue rulings, or revenue procedures for publishing guidance on Internal Revenue Code provisions. Because of time constraints in publishing such rulemaking documents on the act's provisions, IRS put significantly more emphasis on publishing interpretative guidance in its announcements and notices. In December 1987, IRS announced that taxpayers could rely on interpretative guidance provided in its announcements and notices.

Results in Brief

To implement the act, IRS developed a priority list of act sections that, in its opinion, required some type of early interpretative guidance. IRS' implementation plan provided for publishing 135 regulations, 25 revenue rulings, 13 revenue procedures, 33 notices, and 11 announcements. Of these 217 total issuances, 174 were planned to be published before January 1988.

As of December 31, 1987, 81 of the 92 regulations and all of the 13 revenue procedures planned for publication before the 1988 filing season were still in process. Some of these regulations and revenue procedures were subsequently published during the 1988 filing season, but by April 30, 1988, 51 regulations and 3 revenue procedures were still pending. By April 17, 1989, 21 of these regulations were published and another 4 were deleted.

In contrast, 14 of the 25 revenue rulings, 28 of the 33 notices, and 10 of the 11 announcements scheduled for early publication were published in time for the filing season and nearly all had been issued by April 30, 1988. In addition, as IRS gained familiarity with the Act, it shifted some priorities and went on to publish an additional 22 regulations, 10 revenue rulings, 9 revenue procedures, 77 notices, and 78 announcements not included in the original implementation plan by the end of April 1988.

The sufficiency of the interpretative guidance provided to taxpayers will probably not be known for another year or two, pending results of IRS audits of tax returns subject to the act. However, IRS Internal Audit staff who monitored the 1988 filing season, said they did not identify any problems that could be attributed to insufficient interpretative guidance.

As a result of the lessons learned from issuing a revised Form W-4 without obtaining comments from the general public, IRS pretested new and revised tax forms before they were published in final form, and made some changes on the basis of comments received.

Objectives, Scope, and Methodology

To obtain information on IRS' interpretative guidance, we (1) analyzed the interpretative guidance action items in IRS' implementation plan; (2) monitored IRS' efforts concerning these action items; (3) identified some implementation actions, other than those in the plan, that IRS took to provide interpretative guidance; and (4) held discussions with IRS officials and tax practitioners.

We did our work from October 1987 through April 1989 and in accordance with generally accepted government auditing standards.

IRS Developed Priorities for Providing Interpretative Guidance

The Tax Reform Act added, changed, or repealed over 2,000 subsections of the Internal Revenue Code. Most of the act's provisions were either effective upon its enactment or apply to taxable years beginning after December 31, 1986.

On October 23, 1986, a day after the statute was enacted, IRS published a priority list of 76 act sections which, in its opinion, needed some type of early interpretative guidance. IRS' selection of these sections, according to IRS' Chief Counsel, was based on such factors as the relative number of affected taxpayers, the extent of change from prior Code provisions, the relative need to explain a new requirement, and IRS' operational requirements.

In June 1987, IRS adopted a plan containing over 2,000 action items that IRS believed it needed to complete to implement the act. Of these items, 217 required publication of some type of interpretative guidance. About 64 percent of the 217 items pertained to the 76 high-priority act sections.

Most of the interpretative guidance items (174) were scheduled to be published before January 1988—in time for the 1988 filing season, as shown in table 1.

Table 1: Interpretative Guidance That IRS Planned to Publish

Type of guidance	Number	To be published before January 1988
Regulation ^a	135	92
Revenue ruling	25	25
Revenue procedure	13	13
Notice	33	33
Announcement	11	11
Total	217	174

^aForty-three regulations were scheduled for publication at various times after December 1987. Source: IRS Implementation Plan for the Tax Reform Act of 1986 (Public Law 99-514), June 1987.

Other Types of Guidance Were Provided but Most Regulations Scheduled for Early Publication Were Pending

As of December 31, 1987, 81 of the 92 regulations and all of the 13 revenue procedures scheduled for publication before the 1988 filing season were still in process. In contrast, most of the revenue rulings, notices, and announcements scheduled for early publication were published in time for the filing season. The status of the interpretative guidance scheduled for early publication is shown in table 2.

Table 2: Status of Interpretative Guidance Scheduled for Publication Before 1988 Filing Season

Type of guidance	Planned	Published		Total	Deleted	Pending as of	
		Before filing season	During filing season ^a			April 1988	April 1989
Regulation	92	11	28	39	2	51	26
Revenue ruling	25	14	9	23	1	1	1
Revenue procedure	13	0	7	7	3	3	3
Notice	33	28	2	30	0	3	2
Announcement	11	10	0	10	0	1	1
Total	174	63	46	109	6	59	33

^aJanuary 1 through April 30, 1988

Regulations scheduled for publication were in various stages of completion as of April 30, 1988. Of 51 regulations, 39 were in process at IRS, 7 were at Treasury for initial review, and 5 were awaiting final approval by Treasury. IRS officials attribute the difference between the number of regulations published and the number planned to (1) the difficulties in resolving all the issues necessary to publish complete regulations and (2) shifts in publication priorities due to IRS' views that forms and other publications provided sufficient guidance pending issuance of the regulations.

Subsequently, 21 of the 51 pending regulations were published (May 1, 1988, through April 17, 1989) and 4 were deleted from the plan. Except for the deletion of one notice, the remaining pending interpretative guidance had not been issued as of April 17, 1989.

In addition to publishing the planned items shown in table 2, IRS published more interpretative guidance than it had scheduled. An additional 22 regulations (proposed, temporary, or final), 10 revenue rulings, 9 revenue procedures, 77 notices, and 78 announcements that were not

included in IRS' original implementation plan were published by the end of April 1988.

IRS officials said the primary reason for this increase was the difficulty in anticipating all the issues that needed to be addressed during the implementation period for the act. In responding to the increased number of issues that needed to be addressed, IRS issued announcements and notices that focused on individual issues and which could be published quickly.

The sufficiency of the interpretative guidance provided to taxpayers will probably not be known for another year or two, pending results of IRS audits of tax returns subject to the act. However, IRS Internal Audit staff, who monitored the 1988 filing season, said they did not identify problems that could be attributed to insufficient interpretative guidance. Representatives of the American Bar Association believe IRS did a good job in publishing the guidance. Representatives of the American Institute of Certified Public Accountants gave IRS a generally favorable review.

Form W-4 Lessons Learned Were Applied to Other Activities

As a result of complaints it received after publishing a revised Form W-4 without obtaining public comments, IRS obtained broader public comments on new or revised tax forms. IRS published draft tax forms in the Federal Register and newspapers. To get taxpayers' reactions, IRS met with groups comprising a cross-section sample of taxpayers. In the past, IRS obtained comments primarily from tax experts, practitioner groups, and the Office of Management and Budget.

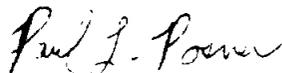
IRS considered public comments in deciding on forms and filing requirements for implementing the act. This process had positive results. For example, the new form for reporting residential interest (Form 8598—Home Mortgage Interest) and the form's filing requirements were both revised, partly on the basis of public reaction. By changing the filing requirements so that the form applied to only a limited number of taxpayers, IRS significantly reduced the burden on taxpayers as well as the number of forms it had to process.

IRS also obtained taxpayers' reactions to several of the most commonly used forms: Forms 1040, 1040A, 1040EZ, Schedule A for Form 1040, and Form 8606—Nondeductible IRA Contributions. As a result, IRS

gained early insights into the sources of taxpayer confusion in completing forms and received suggestions for changing the forms to minimize these problems.

As agreed with your offices, IRS officials were given an opportunity to review a draft of this report, and they suggested some clarifications, which we have made. We are sending copies of this report to the Commissioner of Internal Revenue, the Chief Counsel of IRS, and other interested parties and will make copies available to others upon request.

The major principal contributors to this report are listed in the appendix. If you have any questions concerning this report, please call me on 272-7904.



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